



REPORT OF THE AUDITOR-GENERAL TO THE NORTH WEST PROVINCIAL LEGISLATURE AND THE COUNCIL OF THE NALEDI LOCAL MUNICIPALITY

REPORT ON THE FINANCIAL STATEMENTS

Introduction

1. I have audited the financial statements of the Naledi Local Municipality set out on pages XX to XX, which comprise the statement of financial position as at 30 June 2013, the statement of financial performance, statement of changes in net assets and the cash flow statement for the year then ended and the notes, comprising of a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP), the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA), the Division of Revenue Act of South Africa, 2012 (Act No. 5 of 2012) (DoRA) and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-General's responsibility

3. My responsibility is to express an opinion on these financial statements based on my audit. I conducted my audit in accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA), the General Notice issued in terms thereof and International Standards on Auditing. Those standards require that I comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.
4. An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.
5. I believe that the audit evidence I have obtained is sufficient and appropriate to provide a basis for my unqualified audit opinion.

Opinion

6. In my opinion, the financial statements present fairly, in all material respects, the financial position of the Naledi Local Municipality as at 30 June 2013, and its financial performance and cash flows for the year then ended in accordance with SA Standards of GRAP and the requirements of the MFMA and the DoRA.

Emphasis of matters

7. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Restatement of corresponding figures

8. As disclosed in note 34 to the financial statements, the corresponding figures for the year ending 30 June 2012 have been restated as a result of errors discovered at, and for the year ended, 30 June 2013.

Unauthorised, irregular and fruitless and wasteful expenditure

9. As disclosed in note 35.1 to the financial statements, unauthorised expenditure of R61 898 112 was incurred in the current year and unauthorised expenditure in respect of prior years of R87 744 433 has not yet been dealt with in accordance with section 32 of the MFMA.
10. As disclosed in note 35.2 to the financial statements, fruitless and wasteful expenditure of R12 745 560 was incurred in the current year and fruitless and wasteful expenditure in respect of prior years of R33 834 705 has not yet been dealt with in accordance with section 32 of the MFMA.
11. As disclosed in note 35.3 to the financial statements, irregular expenditure of R7 993 025 was incurred in the current year and irregular expenditure from prior years of R130 547 938 has not yet been dealt with in accordance with section 32 of the MFMA.

Impairments and material losses

12. As disclosed in note 2 to the financial statements, impairments of R174 430 569 (2012: R155 720 825) were incurred as a result of significant impairments of debtors.
13. As disclosed in note 27 to the financial statements, material distribution losses of R14 870 779 (2012: R13 067 426) and R4 928 336 (2012: R652 277) respectively were incurred as a result of electricity and water losses.

Going concern

14. The statement of financial performance indicates that the Naledi Local Municipality incurred a net loss of R88 471 841 (2012: R53 754 800) during the year ended 30 June 2013 and, as of that date, the municipality's current liabilities exceeded its current assets by R191 706 940. These conditions, along with other matters as set forth in note 45 indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern.

Additional matter

15. I draw attention to the matter below. My opinion is not modified in respect of this matter.

Unaudited supplementary schedules

16. The supplementary information set out on pages XX to XX does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly I do not express an opinion thereon.

REPORT ON OTHER LEGAL AND REGULATORY REQUIREMENTS

17. In accordance with the PAA and the *General Notice* issued in terms thereof, I report the following findings relevant to performance against predetermined objectives, compliance with laws and regulations and internal control, but not for the purpose of expressing an opinion.

Predetermined objectives

18. I performed procedures to obtain evidence about the usefulness and reliability of the information in the annual performance report as set out on pages XX to XX of the annual report.



19. The reported performance against predetermined objectives was evaluated against the overall criteria of usefulness and reliability. The usefulness of information in the annual performance report relates to whether it is presented in accordance with the National Treasury's annual reporting principles and whether the reported performance is consistent with the planned development priorities or objectives. The usefulness of information further relates to whether indicators and targets are measurable (i.e. well defined, verifiable, specific, measurable and time bound) and relevant as required by the National Treasury Framework for managing programme performance information (FMSSI).
20. The reliability of the information in respect of the selected development objectives is assessed to determine whether it adequately reflects the facts (i.e. whether it is valid, accurate and complete).
21. The material findings are as follows:

Usefulness of information

22. Section 46 of the Municipal Systems Act, 2000 (Act No 32 of 2000) (MSA) requires disclosure in the annual performance report of measures taken to improve performance where planned targets were not achieved. Adequate and reliable corroborating evidence could not be provided for 41% of the measures taken to improve performance as disclosed in the annual performance report. The municipality's records did not permit the application of alternative audit procedures and this was due to limitations placed on the scope of my work. Consequently, I did not obtain sufficient appropriate audit evidence to satisfy myself as to the reliability of the measures taken to improve performance.

Reliability of information

23. The FMSSI requires that institutions should have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of information presented with respect to the following planned development priorities or objectives:
 - To provide roads
 - To provide access to basic refuse removal services
 - Promote access to free basic services to communities
 - To provide electricity
 - To provide adequate water consistently to communities
 - To provide adequate housing

This was due to the fact that the institution could not provide sufficient appropriate evidence in support of the information presented with respect to the objectives.

Compliance with laws and regulations

24. I performed procedures to obtain evidence that the municipality has complied with applicable laws and regulations regarding financial matters, financial management and other related matters. My findings on material non-compliance with specific matters in key applicable laws and regulations as set out in the *General Notice* issued in terms of the PAA are as follows:

Strategic planning and performance management

25. The municipal council did not consult with the local community in the drafting and implementation of the municipality's integrated development plan (IDP), by means of a municipal wide structure for community participation, as required by section 28 of the MSA and Municipal planning and performance management regulation 15(1)(a)(i).
26. The municipality did not afford the local community at least 21 days to comment on the final draft of its IDP before the plan was submitted to council for adoption, as required by Municipal planning and performance management regulation 15(3).



27. The municipality did not give effect to its IDP and conduct its affairs in a manner which was consistent with its IDP, as required by section 36 of the MSA, section 21(2)(a) of the MFMA and Municipal planning and performance management regulation 6.
28. The municipal council did not review its IDP in accordance with an assessment of its performance measurements in terms of section 41 to the extent that changing circumstances demanded as required by section 34 of the MSA and Municipal planning and performance management regulation 3.
29. The performance management system of the municipality was not in line with the priorities, objectives, indicators and targets contained in its IDP and did not clarify the roles and responsibilities of each role-player in the functioning of the system as required by section 38(a) of the MSA and Municipal planning and performance management regulation 7(2)(f).
30. The municipality did not establish mechanisms to monitor and review its performance management system, as required by section 40 of the MSA.
31. The municipality did not set measurable performance targets for the financial year with regard to each of the development priorities and objectives and key performance indicators set out in the IDP, as required by section 41(1)(b) of the MSA and the Municipal planning and performance management regulations 12(1) and 12(2)(e).
32. The municipality did not have and maintain effective, efficient and transparent systems of internal control regarding performance management as required by section 62(1)(c)(i) of the MFMA.

Budgets

33. Expenditure was incurred in excess of the limits of the amounts provided for in the votes of the approved budget, in contravention of section 15 of the MFMA.
34. Monthly budget statements were not submitted to the relevant provincial treasury, as required by section 71(1) of the MFMA.

Annual financial statements, performance and annual reports

35. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets, current assets, liabilities, revenue and disclosure items identified by the auditors in the submitted financial statement were subsequently corrected and the supporting records were provided subsequently, resulting in the financial statements receiving an unqualified audit opinion.
36. The 2011/12 annual report was not made public immediately after the annual report was tabled in the council, as required by section 127(5)(a) of the MFMA.
37. An oversight report, containing comments on the annual report, was not adopted by council within two months from the date on which the 2011/12 annual report was tabled, as required by section 129(1) of the MFMA.
38. The council's oversight report on the 2011/12 annual report was not made public within seven days of its adoption, as required by section 129(3) of the MFMA.

Audit committee

39. The audit committee did not respond to the council on the issues raised in the audit reports of the Auditor-General, as required by section 166(2)(c) of the MFMA.
40. The audit committee did not review all the quarterly internal audit reports on performance measurement, as required by Municipal planning and performance management regulation 14(4)(a)(i).



Internal audit

41. The internal audit unit did not assess the functionality of the performance management system, as required by Municipal planning and performance management regulation 14(1)(b)(i).
42. The internal audit unit did not audit the performance measurements on a continuous basis as required by Municipal planning and performance management regulation 14(1)(c).

Procurement and contract management

43. Goods and services of a transaction value above R200 000 were procured without inviting competitive bids, as required by SCM regulation 19(a).
44. Construction projects were not always registered with the Construction Industry Development Board (CIDB), as required by section 22 of the CIDB Act and CIDB regulation 18.

Expenditure management

45. Money owing by the municipality was not always paid within 30 days or an agreed period, as required by section 65(2)(e) of the MFMA.
46. Reasonable steps were not taken to prevent unauthorised expenditure, irregular expenditure and fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA.

Conditional grants received

47. The municipality did not submit quarterly performance reports to the transferring national officer, the provincial treasury and the National Treasury, within 30 days after the end of each quarter, as required by section 12(2)(c) of the DoRA.
48. The municipality did not evaluate its performance in respect of programmes funded by the Municipal Infrastructure Grant, Integrated National Electrification Programme Grant, Local Government Financial Management Grant and Municipal Systems Improvement Grant within two months after the end of the financial year, as required by section 12(5) of the DoRA.
49. The municipality did not timeously submit project registration forms, for projects it intends implementing in the financial year 2013/14, to the department of local government, as required by the Division of Revenue Grant Framework, Gazette No. 35399.
50. The municipality did not submit project implementation plans to the national department (CoGTA), as required by the Division of Revenue Grant Framework, Gazette No. 35399.
51. The municipality did not register its master plans for bulk infrastructure with the Integrated National Electrification Programme, as required by the Division of Revenue Grant Framework, Gazette No. 35399.
52. The municipality did not submit MFMA implementation plans to National Treasury to address weaknesses in financial management, as required by the Division of Revenue Grant Framework, Gazette No. 35399.
53. The municipality did not submit its signed activity plan to the national department (CoGTA), as required by the Division of Revenue Grant Framework, Gazette No. 35399.
54. The municipality did not submitted, within 10 days after the end of each month, its monthly expenditure reports to the national department (CoGTA), as required by the Division of Revenue Grant Framework, Gazette No. 35399.

Consequences management

55. Unauthorised, irregular and fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, in accordance with the requirements of section 32(2) of the MFMA.

Human resource management

56. The competencies of financial and supply chain management officials were not assessed promptly in order to identify and address gaps in competency levels as required by the Municipal Regulations on Minimum Competency Levels regulation 13.
57. The municipality did not submit a report on compliance with prescribed competency levels to the National Treasury and relevant provincial treasury as required by the Municipal Regulations on Minimum Competency Levels regulation 14(2)(a).
58. The annual report of the municipality did not reflect information on compliance with prescribed minimum competencies as required by the Municipal Regulations on Minimum Competency Levels regulation 14(2)(b).

Waste management

59. The municipality operated its waste disposal sites and wastewater treatment facilities without a license or permit in contravention of section 20(b) of the National Environmental Management Waste Act, 2008 (Act No. 59 of 2008) (NEMWA), section 24(2)(a) of the National Environmental Management Act, 1998 (Act No. 107 of 1998) (NEMA), section 20(1) of the Environmental Conservation Act, 1989 (Act No. 73 of 1989) (ECA) and section 22(1)(b) of the National Water Act, 1998 (Act No. 36 of 1998) (NWA).
60. The municipality's operational activities at its waste disposal sites and wastewater treatment facilities contravened or failed to comply with the requirements of a waste management permit or license and the regulatory provisions in terms of section 67(1)(f) and (h) of the NEMWA and section 29(4) of the ECA in instances where such were issued.
61. The municipality's waste management and disposal activities contravened or failed to comply with the requirements of section 28(1) of the NEMA, section 19 of the NWA and sections 16(1)(c) and (d) and 26(1)(b) of the NEMWA.

Internal control

62. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with laws and regulations. The matters reported below under the fundamentals of internal control are limited to the findings on the annual performance report and the findings on compliance with laws and regulations included in this report.

Leadership

63. The municipality has not implemented effective human resource management to ensure that adequate and sufficiently skilled resources are in place and that performance is monitored. Policies and procedures were not communicated to enable and support understanding and execution of internal control objectives, processes and responsibilities as well as to ensure monitoring of compliance with laws and regulations. An information technology (IT) governance framework that supports and enables the business, delivers value and improves performance was not established for the year under review. Appropriate systems and processes for collecting, compiling and reporting on performance against predetermined objectives have not been established and prioritised for the municipality.



Financial and performance management

64. The municipality has not implemented proper record keeping in a timely manner to ensure that complete, relevant and accurate information is accessible and available to support financial and performance reporting. The municipality has placed significant reliance on consultants for financial reporting. The municipality has not prioritised their focus on improving their policies and processes around reporting on performance against predetermined objectives and processes to ensure and monitor compliance with laws and regulations.

Governance

65. The municipality has not implemented appropriate risk management activities to ensure that regular risk assessments, including consideration of IT risks, fraud prevention and compliance with laws and regulations, are conducted and that a risk strategy to address the risks is developed and monitored. The Internal audit function is not adequately identifying and reporting on internal control deficiencies and deficiencies around reporting on predetermined objectives. The audit committee did not ensure accountability and service delivery by evaluating and monitoring responses to risks, furthermore the audit committee did not provide adequate oversight over the effectiveness of the internal control environment.

OTHER REPORTS

Investigations

66. An investigation was conducted by an independent consulting firm on request of the municipality. The investigation was initiated based on the allegation of possible misappropriation by employees, of assets that were received from one of the municipality's subcontractors. The investigation resulted in criminal proceedings being instituted against two employees.

Auditor General .

Potchefstroom

30 November 2013



Auditing to build public confidence